Supreme Court, U.S.
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No. _____

In the Supreme Court of the United States

October Term, 1994

NICHOLAS E. TAVAGLIONE,

Respondent,

v.

MICHAEL C. BILLINGS, MARYANN ARCHAMBAULT, J. RICHARD SWARTZ, ROY E. WHITEHEAD, and RIVERSIDE NATIONAL BANK,

Petitioners.

PETITION FOR WRIT OF CERTIORARI
TO THE CALIFORNIA COURT OF APPEAL

PETITION FOR WRIT OF CERTIORARI

HAIGHT, BROWN & BONESTEEL,
Roy G. Weatherup,* and
Rita Gunasekaran
1620 26th Street, Suite 4000 North
Post Office Box 680
Santa Monica, California 90406-0608
Telephone: (310) 449-6000

Attorneys for Petitioners,
MICHAEL C. BILLINGS, MARYANN ARCHAMBAULT,
J. RICHARD SWARTZ, ROY E. WHITEHEAD,
and RIVERSIDE NATIONAL BANK

*** Counsel of Record**

Westside Law Publishers • West Hollywood, CA 90069 • (310) 273-2887

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QUESTIONS PRESENTED

1. May a state court, consistent with the constitutional requirement of notice, affirm a massive judgment against a federally chartered bank on the basis of an "implied" or "oral" contract to make or renew loans, where no such cause of action was ever pleaded or submitted to the jury?

2. Where a federal statute prohibits a federally chartered bank from loaning money to a borrower who is not credit worthy, may a state require the bank to make such a loan, on pain of civil liability?

LIST OF PARTIES TO THIS PROCEEDING

The only parties to this proceeding are the petitioners, Michael C. Billings, Maryann Archambault, J. Richard Swartz, Roy E. Whitehead, and Riverside National Bank, the defendants in the state courts, and respondent Nicholas E. Tavaglione, the plaintiff below.

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Petitioners.

PETITION FOR WRIT OF CERTIORARI

To the Honorable William H. Rehnquist, Chief Justice of the United States, and to the Honorable Associate Justices of the Supreme Court of the United States:

Petitioners, Michael C. Billings, Maryann Archambault, J. Richard Swartz, Roy E. Whitehead, and Riverside National Bank, respectfully pray that a writ of certiorari be issued to review the decision rendered by the Court of Appeal of the State of California, Fourth Appellate District, Division Two. The Supreme Court of California has denied review. The issues presented include litigants' due process right to notice of claims against them before liability may be imposed by a court of law, and the preemption of a state court ruling which directly conflicts with a federal statute.

THE OPINIONS RENDERED BY THE CALIFORNIA REVIEWING COURTS

On November 17, 1993, the California Court of Appeal affirmed the judgment entered below. The court's opinion is Appendix A to this petition. This decision by the Court of Appeal was rendered upon reversal of its prior decision, and remand of the case to it by the California Supreme Court. *Tavaglione v. Billings*, 4 Cal.4th 1150, 17 Cal.Rptr.2d 608, 847 P.2d 574 (1993). [Appendix B.] The Supreme Court had granted review pursuant to the petition filed by the defendants after the first opinion filed by the California Court of Appeal on June 15, 1992. [Appendix C.]

JURISDICTION

The California Court of Appeal filed its opinion on November 17, 1993. It denied rehearing on December 10, 1993. [Appendix E.]

The defendants' request for review by the California Supreme Court was denied on March 3, 1994. [Appendix D.] On that date, the judgment of the trial court (Appendix F) became final as to the State of California.

The jurisdiction of the Supreme Court of the United States is invoked pursuant to 28 *U.S.C.* section 1257.

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

This petition involves the Fourteenth Amendment to the Constitution of the United States. The relevant portion of this amendment is set forth in Appendix N. The case also involves 12 *U.S.C.* sections 375b and 1818(a)(2) [Appendix M and N], and 12 *C.F.R.* section 215.4(a) and (c). [Appendix O.]

STATEMENT OF THE CASE

1. The Constitutional and Statutory Bases for This Petition for Certiorari.

The second and most recent decision by the California Court of Appeal of the Fourth Appellate District, Division Two, violates the defendants' Fourteenth Amendment due process right to notice of claims against them, and flouts federal statutes prohibiting loans to a deadbeat[1] borrower. The Court of Appeal's decision, which is legally unsustainable, was obviously dictated by the court's determination to reach the same conclusion it had reached prior to remand of the case to it upon review by the California Supreme Court.

Although the court finally recognizes that the plaintiff has no private right to damages for his alleged "illegal ouster" from his position as a director of the Bank, the central claim on which the plaintiff's entire lawsuit is based, it nevertheless affirms. It does so by creating out of thin air an absolute duty on the part of the Bank to renew the plaintiff's overdue loans, purportedly pursuant to an "implied" or "oral" contract.

The Court of Appeal holds that the Bank's refusal to renew the plaintiff's overdue loans constitutes a breach of contract to renew those loans. [Appendix A:39-48.] However, the plaintiff neither pleaded, nor attempted to prove at trial, either the existence of a contract to renew a loan or its breach by the Bank. Accordingly, the Court of Appeal does not, and cannot, point to evidence of an objectively verifiable contract in the pleadings. The court summarily disregards the pleading defect, stating that the plaintiff's "allegation regarding the 'loan

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[1] The word "deadbeat" is defined in *Black's Law Dictionary*, Sixth Edition, West Publishing Company (1990), as "one who fails to pay his debts."

transactions,' although cursory and conclusionary (sic), nevertheless adequately alleges the requisite underlying contract between plaintiff and defendants." [Appendix A:41.]

Not only does the record contain no evidence of any such contract, but it contains ample evidence to the contrary. Each of the loan agreements signed by the plaintiff with the Bank contains a specific provision permitting the Bank to demand immediate repayment of the entire loan in the event of plaintiff's default. [See, for example, 10 J.A. 2666, 2669, 2673, 2681, 2684, 2717.][2]

The lack of evidence at trial, of any contract between the parties to renew a loan, is dealt with equally cavalierly by the court. It concludes that evidence of prior renewals of the plaintiff's loans by the Bank "is sufficient to establish either an oral agreement or an agreement implied from Billings' conduct that defendants, at the very least, would not refuse unreasonably to renew or extend plaintiff's outstanding loans while plaintiff's cash flow problem persisted and so long as plaintiff was current on the interest payments." [Appendix A:42-43.] Such an imposition of liability by a reviewing court, without notice and an opportunity to defend, constitutes a clear violation of the Fourteenth Amendment of the Constitution, and merits intervention by this court.

The decision by the Court of Appeal also conflicts directly with governing federal statutes. Since the Bank is federally chartered, it is governed by the *National Bank Act*, 12 *U.S.C.* section 1 *et seq.* [Appendix H:2, 5.] 12 *U.S.C.* section 375b(3) prohibits loans to bank "insiders" who are less credit worthy than, or on terms not available to, other borrowers. 12 *U.S.C.* section 1818(a)(2) prohibits loans to borrowers

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[2] "J.A." refers to Joint Appendix and "R.T." refers to Reporter's Transcript. The designation is preceded by the volume number, and is followed by the page number.

who are not credit worthy on pain of loss of the Bank's insured status. However, in its blind determination to affirm, the court creates an absolute duty on the Bank's part to renew the plaintiff's loans, regardless of his credit worthiness.

The plaintiff admitted in his operative pleading that, at the pertinent time, he was over 30 days in default on his several loans from the Bank. [Appendix H:4.] The record supports this admission. [11 J.A. 1355; 11 R.T. 2307-2318.] The evidence is also undisputed that the Bank was aware of the severe cash flow problems encountered by the plaintiff at that time. [8 R.T. 1593.]

It is under these circumstances that the Bank prudently refused to renew the plaintiffs' several loans on which he was already in default for over 30 days. Nonetheless, the California Court of Appeal has seen fit to impose a crushing liability on the Bank by creating an absolute duty to renew the plaintiff's overdue loans regardless of his credit worthiness. Such a duty is unheard of in common law and contrary to the governing federal statute. The decision by the Court of Appeal directly conflicts with federal law enacted to protect financial institutions and their depositions, is preempted, and must not be tolerated by this court.

2. The Operative Pleadings.

On May 11, 1987, the plaintiff sued Riverside National Bank, its president, Mr. Michael C. Billings, its chairman of the board of directors, Mrs. Dolores Magnuson, and its other directors, Mrs. Maryann Archambault, Mr. Leon Sigerman, Mr. J. Richard Swartz, and Mr. Roy E. Whitehead.[3] [Appendix H:2.] In the operative first amended complaint, the plaintiff asserted seven causes of action, including "illegal ouster" of

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[3] Mrs. Magnuson and Mr. Sigerman are not parties to this appeal.

plaintiff as a director, defamation, wrongful disclosure of confidential information, breach of the implied covenant of good faith and fair dealing, interference with contractual relationships, interference with contractual relations and prospective advantage, and negligent interference with contractual relationships. [Appendix H:2-19.]

In the fourth cause of action, for breach of the implied covenant of good faith and fair dealing, the plaintiff claimed that the defendants had breached the covenant by improperly removing him as a director of the corporation; by failing to give him an opportunity to cure his loan defaults, prior to adoption of the bylaw; by utilizing his illegal ouster from the board as a pretense for subsequently publishing confidential and private information concerning his loan accounts and defaults; and by formulating and implementing a plan to force him into selling his shareholdings in the Bank. [Appendix H:12-14.] In this entire cause of action, there was absolutely no mention of any contract between the plaintiff and the Bank, much less one whereby the Bank unequivocally agreed to renew the plaintiff's loans, regardless of his credit worthiness. [Appendix H:12-14.]

3. The Overruling of the Demurrer and the Answer Filed by the Defendants.

The defendants demurred to the plaintiff's first amended complaint. [Appendix I.] In demurring to the plaintiff's fourth cause of action for breach of the implied covenant of good faith and fair dealing, the defendants contended that it was impossible to determine the source of the duty of good faith alleged by the plaintiff to be owed to him, since no contract was alleged, and no statutory basis for a good faith duty was set forth by him.

However, the trial court overruled the defendants' demurrer [Appendix J] and the defendants filed an answer to the complaint. [Appendix K.]

4. The Poor Excuse for a Trial.

The trial court ignored the fundamental problem that plaintiff's entire suit rests upon the supposed violation of his supposed right to remain in office as a director of the Bank, a primary right that does not exist. Moreover, there is no wrongful act or omission alleged that is not related to the plaintiff's removal as a director, and there is no item of damages claimed to have been caused by separate or independent conduct. The trial court refused to accept this plain fact, and permitted a legally meritless suit to go to the jury. There was also no mention throughout the trial of the existence of any type of contract between the Bank and the plaintiff to renew his loans automatically, regardless of whether or not he was in default, and without taking into consideration his credit worthiness at the time the loans became due.

5. The Jury Verdict and the Judgment.

In the judgment entered pursuant to the jury verdict, the court awarded the plaintiff $2,254,787.00 in compensatory damages and $2,300,000.00 in punitive damages against the Bank; $2,254,787.00 in compensatory damages and $130,000.00 in punitive damages against Mr. Michael Billings; and $1 each from Mr. J. Richard Swartz, Ms. Maryann Archambault, and Mr. Roy E. Whitehead. [Appendix F].

6. The First Erroneous Decision Filed by the Court of Appeal.

The defendants appealed from the judgment entered against them, raising 22 distinct issues on appeal[4] including their central defense that plaintiff's removal from his fiduciary position as director of the Bank simply could not entitle him to a private suit for damages.

Interestingly, in its first opinion, the Court of Appeal recognized that the "plaintiff's complaint . . . did not allege separate causes of action which would independently support separate damage awards but instead alleged one cause of action, framed in separate counts, asserting various theories of recovery based upon the same operative facts." [Appendix C:16.] Nevertheless, the court did not stop to consider whether plaintiff's central claim for wrongful ouster was legally sustainable. Instead, relying on the general verdict rule, and ignoring the numerous instructional and evidentiary errors pointed out by the defendants, the court affirmed the erroneous judgment entered below.

Candidly acknowledging its inability "to comprehend the function or import of the special interrogatories regarding damages," (Appendix C:16) the court affirmed the entire $2.25 million judgment ignoring the jury's finding that the plaintiff had incurred only $604,787.00 in compensatory damages from defendants' defamation.

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[4] Included among them was the threshold issue of the trial court's jurisdiction since, under California law, the director of a bank questioning his removal from the board by the enactment of a bylaw, is required to proceed solely by an action in the nature of *quo warranto*. California *Code of Civil Procedure* sections 801-811.

7. The California Supreme Court's Decision Upon Review, and the Remand of the Case to the Court of Appeal.

The California Supreme Court granted the defendants' petition for review of the Court of Appeal's erroneous decision expressly stating: "We disagree with the Court of Appeal's analysis." [Appendix B:10.] It found the "Court of Appeal's statement that the damage interrogatories were 'meaningless and irrelevant' . . . *puzzling*." [Appendix B:10.] It held that the Court of Appeal's limited review of issues relating to the defamation claim could not sustain the entire $2.25 million judgment, and reversed and remanded. [Appendix B:10.]

8. The Court of Appeal's Second Erroneous Decision Which Violates the Defendants' Constitutionally Protected Right to Notice, and Conflicts With Federal Law.

The second decision filed by the Court of Appeal is even more grievously flawed than the first. [Appendix A.] Determined to affirm the erroneous judgment, the court stubbornly states: "While we share defendants' view that plaintiff's first purported cause of action for damages based on defendants' 'illegal ouster' or removal of plaintiff from the RNB board of directors does not, as a matter of law, state a theory of recovery which supports an award of damages, we shall not address that issue, or any of the defendants' other challenges to that cause of action. Even if we were to conclude plaintiff's recovery under the first cause of action was, for some reason, invalid, that conclusion would not require reversal of the entire judgment in view of the jury's liability and damage findings in connection with plaintiff's other theories of recovery." [Appendix A:16.]

Reasoning thus, the Court of Appeal chooses to address only the defamation and breach of the implied covenant of good faith and fair dealing causes of action. The Court of Appeal fails to grasp the interrelationship between the invalid "illegal ouster" cause of action, and the two causes of action which the court finds sufficient to support the judgment against the defendants.

Once it is acknowledged that there can be no private cause of action for the alleged "illegal ouster" of a bank director, the viability of plaintiff's suit against the Bank is dependent upon a legally untenable duty to make loans to the plaintiff. Since there can be no such legal duty, the Court of Appeal has attempted to create one. The court announces that the plaintiff's "allegation regarding the 'loan transactions,' although cursory and conclusionary (sic), nevertheless adequately alleges the requisite underlying contract between plaintiff and defendants." [Appendix A:41.] It then rules that the evidence was "sufficient to establish either an oral agreement or an agreement implied from Billings's conduct that defendants, at the very least, would not refuse unreasonably to renew or extend plaintiff's outstanding loans while plaintiff's cash flow problem persisted and so long as plaintiff was current on the interest payments." [Appendix A:42-43.]

9. The Denial of the Petition for Rehearing.

The defendants filed a petition for rehearing on December 2, 1993. [Appendix G.] The defendants contended that, in apparent recognition of the fact that the plaintiff's entire case depends upon the Bank's supposed duty to make loans to the plaintiff, the court has attempted to create such a duty, because no such legal duty exists. However, since there is not even a suggestion of a breach of contract action in the record, and federal law prohibits loans to borrowers who are not credit worthy, the court's creation of an absolute duty to

renew the plaintiff's loans violates the defendants' constitutionally protected due process right to notice embodied in the Fourteenth Amendment and conflicts with federal statutes, such as 12 *U.S.C.* section 1818, prohibiting loans to borrowers who are not credit worthy.[5] [Appendix G:2-5.] In compliance with rule 14(h) of the *Rules of the Supreme Court of the United States*, it is pointed out that it was in this manner that the defendants raised the constitutional issue of notice, as well as the conflict created by the Court of Appeal decision with governing federal statutes. The Court of Appeal denied the defendants' petition for rehearing on December 10, 1993. [Appendix E.]

10. The California Supreme Court's Denial of the Petition for Review.

Upon denial of the petition for rehearing by the California Court of Appeal, the defendants sought review from the California Supreme Court. The defendants stated that the

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[5] The superior court file in this action contains ample evidence of plaintiff's lack of credit worthiness, which continues to this day. The entire judgment awarded in plaintiff's favor totals $6,939,577.00. However, in keeping with his tendency to borrow far more than he can possibly repay, the plaintiff has given eight voluntary liens against the judgment in his favor, in a total amount of $9,538,507.55. The largest of the lienholders is Chemical Bank, successor by merger to Manufacturers Hanover Trust Company, which has a lien in the amount of $5,896,814.36. In conflict with the prior liens, on March 11, 1994, the plaintiff also assigned to his attorneys 35 percent of all of the proceeds of the judgments, including the interest on those amounts, as well as a November 1, 1990, promissory note for $86,500.00 and the interest accrued thereon. Since the plaintiff has signed all of the liens, it appears that they are voluntary contractual liens within the meaning of California *Civil Code* section 2881(1), rather than liens created by operation of law. The liens are, of course, subject to judicial notice pursuant to California *Evidence Code* sections 452, 453, and 459. Unfortunately, despite the defendants' request, the Court of Appeal refused to take judicial notice of the liens.

Court of Appeal, which finally recognized the invalidity of the plaintiff's "wrongful ouster" claim, invented a whole new theory, breach of contract to make a loan, to once again uphold the judgment. The defendants contended that, in the absence of any allegations in the pleadings and any evidence at trial, of breach of an existing contract with the plaintiff by the Bank, the creation of such a duty by the Court of Appeal constituted a clear violation of the defendants' due process right to notice as guaranteed by the Fourteenth Amendment of the United States Constitution. [Appendix L.]

The defendants also contended that, since the plaintiff was an obvious credit risk at the pertinent time, any contract to make a loan by the Bank would violate federal law as embodied in 12 *U.S.C.* section 1818, which prohibits loans to borrowers who are not credit worthy. [Appendix N.] Unfortunately, all these contentions fell on deaf ears, and the defendants' petition for review was denied. [Appendix D.]

ARGUMENT

I.

Upon Reversal and Remand of the Case by the California Supreme Court, the Court of Appeal Has Once Again Affirmed the Erroneous Judgment by Conjuring Up a Legally Untenable "Implied" or "Oral" Contract to Make or Renew Loans, Ignoring the Total Absence of Such a Contract in the Record, and Has Thereby Trampled the Defendants' Constitutionally Protected Right to Notice of Claims Against Them.

The critical issue in this case, both at trial and when the case was on appeal the first time, was the validity of the plaintiff's first cause of action for "illegal ouster" from his position as a director of the Bank, and pursuant to which he recovered massive damages. While the invalidity of this claim was the primary focus of the defense, it was consistently ignored both by the trial court and by the Court of Appeal.

Upon reversal and remand of the case by the California Supreme Court, which found that there are "substantial issues underlying plaintiff's theory of illegal ouster" [Appendix B:12-13], the Court of Appeal has belatedly recognized that plaintiff's primary cause of action for " 'illegal ouster' . . . does not, as a matter of law, state a theory of recovery which supports an award of damages." [Appendix A:16.]

Once it is acknowledged that plaintiff has no legally tenable cause of action for his alleged "illegal ouster" from the Bank's board, the conclusion is inescapable that the entire lawsuit, which was tried on the premise that the plaintiff stated a valid claim against the Bank for such alleged "illegal ouster," was tainted. The vast body of evidence admitted to support that untenable cause of action, and the numerous jury

instructions given on that issue, were all in error, highly prejudicial, and warrant an immediate reversal. The Court of Appeal, however, refuses to acknowledge the inescapable legal effect of such recognition, and declares:

> "[W]e shall not address that issue, or any of defendants' other challenges to that cause of action." [Appendix A:16.]

As a result of this erroneous conclusion, the Court of Appeal once again upholds the multimillion dollar judgment against the defendants, but does so this time by judicially creating a cause of action which was neither pleaded nor proved at trial. As pleaded, the cause of action for breach of the implied covenant of good faith and fair dealing is based upon the plaintiff's former relationship with the Bank as a stockholder, a director, and a borrower. These three relationships are alleged to create a duty on the part of the Bank and its officers and directors to permit the plaintiff to continue in office as a director. In relation to his position as a borrower, plaintiff's only contentions are that the defendants had a duty to deal "fairly and in good faith" in connection with his loan transactions, and that they failed to give him an opportunity to cure his loan defaults prior to the adoption of the bylaw. [Appendix H:13-14.]

There are absolutely no allegations in the pleadings of the breach of any actual contract between the defendants and the plaintiff, and no such evidence was offered at trial. This fact is implicitly acknowledged by the Court of Appeal, which relies on prior renewals of the plaintiff's loans by the Bank, and states:

> "That evidence, in our view, is sufficient to establish either an oral agreement or an agreement implied from Billings' conduct that defendants, at the very least, would not refuse unreasonably to renew or extend plaintiff's

> outstanding loans while plaintiff's cash flow problem persisted and so long as plaintiff was current on the interest payments. In other words, there was evidence of an established course of conduct or implied contract between plaintiff and defendants which created a duty on the part of the defendants to act in good faith and deal fairly with plaintiff in connection with renewing plaintiff's loans." [Appendix A:42-43.]

In effect, the Court of Appeal has created a fictional, legally untenable, contract to make a contract, whereby it imposes an absolute duty on the Bank to renew the plaintiff's loans, regardless of whether or not he was current on his loan repayments, and without any consideration as to his credit worthiness at the time the loans were to be renewed. Thus, the defendants never had any notice of an obligation to respond to such a cause of action, even if such a cause of action were legally recognized in California, which it is not.

Contrary to the Court of Appeal's finding of an "implied" or "oral" contract to renew the plaintiff's loans, each of the loan agreements signed by the plaintiff with the Bank contains a specific provision permitting the Bank to demand immediate repayment of the entire loan, in the event of a default by the plaintiff. The pertinent portion of the agreements reads:

> "If Borrower does not pay as agreed, or if Borrower or any guarantor of this note breaches any other agreement with the Bank, Borrower will be in default. Upon default, the Bank may declare the entire unpaid principal and accrued interest immediately due, without notice, and Borrower will then pay that amount." [See, for

> example, J.A. 10, 2666, 2669, 2673, 2681, 2684, 2717.]

As recognized in *Groos National Bank v. Comptroller of Currency*, 573 F.2d 889 (5th Cir. 1978), no person can claim a constitutionally protected right to do business with a particular bank. A bank's right to decline or terminate a deposit relationship is well established at common law. 573 F.2d at 897. Consequently, under settled legal principles, there can be no "implied" contract between a bank and its customer to renew the customer's loans regardless of his credit worthiness at the time he seeks to borrow money. Furthermore, even if there is evidence that could support a breach of contract theory, which defendants deny, the present Court of Appeal opinion is improper. For, if the defendants are subject to liability for breach of contract, they had a constitutional right to notice of the claim.

A classic statement of the constitutional right to notice can be found in *Lambert v. People of the State of California*, 355 U.S. 225 (1957). In *Lambert*, this Court declared that:

> "Ingrained in our concept of due process is the requirement of notice. Notice is sometimes essential so that the citizen has the chance to defend charges. Notice is required before property interests are disturbed, before assessments are made, before penalties are assessed." 355 U.S. at 228.

This Court also observed that the requirement of notice applies to both civil and criminal cases. 355 U.S. at 228.

To be constitutionally sufficient, adequate notice must be given of legal proceedings, which must be reasonably calculated to inform parties of those proceedings which may directly and adversely affect their legally protected interests. *Walker v. City of Hutchinson*, 352 U.S. 112, 115-116 (1956).

See also, *Covey v. Town of Somers*, 351 U.S. 141 (1956). The requirement of notice includes fair warning of what the law prohibits. *Bouie v. City of Columbia*, 378 U.S. 347 (1964). In addition, the particular conduct said to violate the law must be specified. *Stirone v. United States*, 361 U.S. 212 (1960); *Russell v. United States*, 369 U.S. 749 (1962).

In *Mullane v. Central Hanover Bank & Trust Company*, 339 U.S. 306 (1950), this Court overturned a state court decree settling accounts by the trustee of a common trust fund, on the ground that the notice given under state law was insufficient to satisfy the requirements of the Fourteenth Amendment. It was observed that "[m]any controversies have raged about the cryptic and abstract words of the Due Process Clause but there can be no doubt that at a minimum they require that deprivation of life, liberty or property by adjudication be preceded by notice and opportunity for hearing appropriate to the nature of the case." 339 U.S. at 313.

In *Mullane*, the court emphasized that the requirement of notice is not simply notice of the pendency of legal proceedings. Rather, the notice must be sufficiently specific that the party receiving it is able to act in the protection of that party's interests. For example, in *Mullane*, the notice given of a probate hearing was deemed constitutionally defective, because it did not refer to the right of the beneficiaries to have a trustee answer for negligence, and it did not advise the beneficiaries that their recoveries might be diminished by attorney's fees that could be challenged. 339 U.S. at 313.

As noted above, the requirement of notice applies equally in civil and criminal cases. The civil equivalent of a criminal indictment is a complaint. Although this Court "has endorsed the modern relaxation of pleading rules, it has never receded from the requirement that civil complaints provide parties defendant with 'fair notice' of the claims against them." *New Motor Vehicle Board of the State of California v. Orrin*

W. Fox Company, 439 U.S. 96, 125, *fn.* 29 (1978) (Dissenting opinion of Justice John Paul Stevens, citing the unanimous opinion of the court in *Conley v. Gibson*, 355 U.S. 41 (1957)).

The principle that notice is an essential part of the concept of due process of law was recently reaffirmed in *United States v. James Daniel Good Real Property*, ___ U.S. ___, 114 S.Ct. 492 (1993). It was held in that case that the government, in a civil forfeiture case, may not seize real property "without first affording the owner notice and an opportunity to be heard." ___ U.S. at ____, 114 S.Ct. at 497. Citing the seminal case of *Mullane v. Central Hanover Bank & Trust Company*, 339 U.S. 306 (1950), and other authorities, the majority observed that "[o]ur precedents establish the general rule that individuals must receive notice and an opportunity to be heard" before they are deprived of property. ___ U.S. at ___, 114 S.Ct. at 4978. In fact, "[t]he right to prior notice and a hearing is central to the Constitution's command of due process." ____ U.S. at _____, 114 S.Ct. at 500.

This constitutionally protected right to notice was violated in this case by the Court of Appeal. Before the defendants can be held liable for breach of a contract, they should have been given notice of such a claim, but they were not. With notice, the defendants could have presented evidence to show the invalidity of the theory. Certainly, the defendants have a constitutional right to defend themselves against any claim of breach of contract. However, they were never given the opportunity to do so.

The Court of Appeal has now upheld a multimillion dollar judgment, relying on an unpleaded cause of action, which was also not proved at trial. Consequently, the defendants had no notice of this supposed "oral" or "implied" contract to renew a loan which they allegedly breached. The defendants' constitutional right to notice of the applicable law

and notice of the factual nature of the conduct charged has been violated. This unconscionable violation of the defendants' inalienable right should not be tolerated by this court. This court should intervene, uphold the rule of law, and protect the defendants' constitutionally guaranteed right to notice, since the California reviewing courts failed to do so.

The focus of the entire trial, and of the first appeal, was plaintiff's "illegal ouster" claim. The plaintiff's operative complaint shows the close interrelationship of the various causes of action, all of which flow from the invalid claim of "illegal ouster." Indeed, all of the allegations of the first cause of action, "illegal ouster," are incorporated into each remaining cause of action. In their appellants' opening brief, the defendants pointed out that all the other causes of action alleged by the plaintiff flowed from his central allegation of "illegal ouster." [Appellants' opening brief at page 50.] In his brief on the merits, the plaintiff acknowledged that he has one cause of action based on a set of operative facts, which is framed in separate counts, asserting various theories of recovery. [Plaintiff's brief on the merits at page 3.] Therefore, by recognizing the invalidity of the "illegal ouster" claim, the Court of Appeal has undermined all of the subsidiary claims. Inexplicably, the Court of Appeal fails to grasp the interrelationship between this invalid cause of action and the two causes of action which it finds sufficient to support the judgment.

The defamation claim rests upon the contention that the plaintiff was not, in fact, validly removed from the board of directors of Riverside National Bank, contrary to what was reported in the press. If the removal of the plaintiff from the board of directors of the Riverside National Bank was not actionable, then it was not defamatory to report the removal. Therefore, now that the Court of Appeal has held, as a matter of law, that plaintiff's "illegal ouster" cause of action does not

state a theory of recovery which supports an award of damages, the defamation claim also cannot stand.

Similarly, if there was never any duty to renew or make loans to the plaintiff, and the record shows that he was undoubtedly in default on his loans, there was nothing defamatory in reporting this fact to the news media. Also, if there is no legally cognizable claim for ousting a delinquent director, then no covenant of good faith and fair dealing arises with respect to the status of the plaintiff as a director. Also, as seen previously, there can be no legally tenable contract to enter into a future loan agreement between the Bank and the plaintiff. In the absence of a contract there can, of course, be no breach of the covenant of good faith and fair dealing. *Peterson Development Company v. Torrey Pines Bank*, 233 Cal.App.3d 103, 116, 284 Cal.Rptr. 367, 375 (1991) *review denied* (1991); *Careau & Company v. Security Pacific Credit, Inc.*, 222 Cal.App.3d 1371, 1393, 1401, 272 Cal.Rptr. 387.

In the present case, the defamation claim was in no way independent of the claim for breach of the covenant of good faith and fair dealing (failure to renew a loan) and the baseless cause of action for "wrongful ouster." Only if there was a duty to renew the plaintiff's loans could it be said that the newspaper coverage of the plaintiff was factually incorrect. Again, only if the bylaw was invalid could plaintiff's "ouster" from his position as the Bank's director be said to have been wrongful, leading to loss of his privacy and damage to his supposedly good reputation.

The Court of Appeal has failed to recognize that all of the causes of action pleaded flow from the plaintiff's removal as a director of the Riverside National Bank. If the removal was not legally wrongful or actionable, then the remaining causes of action are invalid. Moreover, even if the secondary claims were independent in some sense, they were certainly tainted by the lengthy trial on "illegal ouster."

Under these circumstances, the absence of notice of any possible breach of contract claim is particularly prejudicial. There was absolutely no warning to the defendants that they could be held liable pursuant to a breach of contract claim. The Court of Appeal simply created a new cause of action, out of whole cloth, ignoring the fact that it was neither pleaded nor proved at trial. Such a blatant violation of the defendants' constitutionally protected right to notice should not be permitted to remain undisturbed by this court.

II.

Barring Intervention by This Court, the Defendant Bank Will Be Severely Penalized for Acting Prudently and in Conformity With Federal Laws Prohibiting the Unsound Banking Practice of Making Loans to Uncredit worthy Borrowers.

In an effort to stem the tide of the numerous bank failures caused by the overborrowing of bank funds by directors, officers, and other "insiders," Congress has enacted statutes of a regulatory or prohibitory nature, in order to protect the general public who make banks the depositories of their funds. 49 *A.L.R.3d* 727, 731. 12 *U.S.C.* sections 375b and 1818 are examples of such statutes. 12 *U.S.C.* section 375b(3) provides in relevant part:

> "No member bank shall make any loan or extension of credit in any manner to any of its executive officers or directors . . . unless such loan or extension of credit is made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with other persons and does not involve more than the normal risk of repayment or present other unfavorable features." [Appendix M.]

The implementing regulation of this statute is 12 *C.F.R.* section 215.4(a)(1) and (2). [Appendix O.]

The plaintiff was an extremely high credit risk at the pertinent time. There is ample evidence in the record that plaintiff was delinquent in his loan repayments to the Bank. As of March 1987, the plaintiff was past due for one quarterly interest payment on his $271,405.14 loan from January 30, 1987; three monthly interest payments, and three and a half months in principal on his $350,000.00 loan; three interest payments on his $63,000.00 loan; and his entire $30,000.00 loan which was due to be paid off in full on January 26, 1987. [11 J.A. 3055; 11 R.T. 2307-2318.]

In fact, in his pleadings, the plaintiff readily admits that, "[a]s of February 3, 1987, plaintiff had loans from the Bank which had been in default for more than 30 days." [1 J.A. 174.] The record supports this admission. [11 J.A. 1355; 11 R.T. 2307-2318.] Not only was the plaintiff in default on his several loans from the Bank, but he was also encountering severe cash flow problems at that time. The evidence is undisputed that the Bank was aware that plaintiff was no longer credit worthy, and posed a severe risk to the Bank's financial stability, as well as to the financial stability of the Bank's other depositors. [8 R.T. 1593.] It is under these circumstances that the Bank refused to renew the plaintiff's overdue loans. However, under the present decision by the California Court of Appeal, the Bank is being penalized for acting in conformity with federal statutes, taking the plaintiff's lack of credit worthiness into account, and not renewing his loans.

The decision by the Court of Appeal also conflicts with 12 *U.S.C.* section 1818, which provides for the termination of a bank's status as an insured depository institution if, among other grounds:

"[T]he Board of Directors determines that -

> "(i) an insured depository institution or the directors or trustees of an insured depository institution have engaged or are engaging in unsafe or unsound practices in conducting the business of the depository institution;
>
> "(ii) an insured depository institution is in an unsafe or unsound condition to continue operations as an insured institution." [Appendix N.]

Unsafe and unsound banking practices are defined as " 'conduct deemed contrary to accepted standards of banking operations which might result in abnormal risk or loss to a banking institution or shareholder.' " *Northwest National Bank, Fayetteville, Arkansas v. U.S.*, 917 F.2d 1111, 1115 (8th Cir. 1990); *First National Bank of Eden v. Department of the Treasury*, 568 F.2d 610, 611, n. 2 (8th Cir. 1978). For the Bank to have renewed the plaintiff's loans, at the pertinent time, would have constituted an "unsafe and unsound banking practice," under this definition.

Under circumstances such as those present here, reviewing courts have held that the issuance of a Cease and Desist Order by the Comptroller of Currency to a bank to be entirely proper. *First National Bank of Bellaire v. Comptroller of the Currency*, 697 F.2d 674 (5th Cir. 1983), is one such case. The bank in that case made a loan to its senior vice president which exceeded the statutory limits set forth in 12 *U.S.C.* section 375a(2). In response, the Comptroller issued a Cease and Desist Order directing the bank to correct the violation and to implement adequate policies and procedures to ensure that similar violations did not occur in the future. The bank sought to have the order set aside since, subsequent to the making of the loan, the statute was amended making the loan lawful. Nevertheless, the Court of Appeals upheld the validity of the order, declaring:

> "There is undoubtedly a direct relationship between compliance with 12 U.S.C. §375a and a bank's soundness. Even though a subsequent amendment to a statute may correct a violation the amendment does not annul the violation which has already occurred. . . . The Comptroller, consequently, was properly acting within his discretion in issuing a Cease and Desist Order requiring the Bank to implement adequate policies and procedures to ensure that 12 U.S.C. §375a is not violated in the future." (Footnotes deleted.) 697 F.2d at 683.

The decision in *Bullion v. Federal Deposit Insurance Corporation*, 881 F.2d 1368 (5th Cir. 1989), is also illustrative. In that case, the chairman and officers of the board of a bank appealed the assessment of civil penalties against them for violation of section 22(h) of the *Federal Reserve Act*, 12 *U.S.C.* section 375b, and its implementing regulations, 12 *C.F.R.* section 215.4(a) and (c). The chairman of the bank had obtained a $1.5 million loan from the bank for the construction and renovation of townhouses owned by a limited partnership of which he was the general partner. Of relevance here is the discussion regarding violation by the bank's officers of 12 *C.F.R.* section 215.4(a), prohibiting the extension of credit to a bank "insider," such as its director. The *Bullion* court interpreted the enabling provision to prohibit both the extension of preferential terms on loans made to bank "insiders," as well as the maki ‚g of loans which involved more than the normal risk of repayment or presented other unfavorable features. 881 F.2d at 1374. The loan made by the bank in that case to its chairman was found to have violated these prohibitions. The court discussed the various considerations which must be taken into account by a bank making such a loan to an "insider," and emphasized that the "availability of cash to pay off the loan should have been one of the primary consid-

erations of the officers in approving the loan." 881 F.2d at 1375.

Under that criterion, the defendant Bank followed the only possible course open to it when it refused to renew the various loans on which the plaintiff was already in default. The Bank is governed by the *National Bank Act*. Consequently, for it to have acted otherwise, and to have renewed the plaintiff's loans, would not only have been fiscally irresponsible, but would also have been violative of the governing statute. However, the present decision by the Court of Appeal fastens liability on the Bank for acting in compliance with the federal statute. This it should not be permitted to do.

Any state law which interferes with, or is contrary to federal law is, of course, invalid. The supremacy clause of the United States Constitution, Article VI, clause 2, provides:

> "This Constitution and the laws of the United States which shall be made in pursuance thereof . . . shall be the Supreme law of the land; and the judges in every State shall be bound thereby, anything in the Constitution or the laws of any State to the contrary notwithstanding."

In *International Paper Company v. Ouellette*, 479 U.S. 481, 107 S.Ct. 805, 811 (1987), this court recognized that, even where Congress does not speak expressly or impliedly of preemption, state law which actually conflicts with a federal statute or rule is nevertheless preempted to the extent of any conflict. Under that rule, the present Court of Appeal decision which creates a duty on the part of the federally chartered Bank to renew the plaintiff's loans under circumstances which would clearly violate the prohibitions contained in the *National Bank Act* is surely preempted, and should therefore be reversed by this court.

Although no cause of action for breach of contract to make a loan was ever pleaded, certain evidence of the parties' course of conduct with respect to loans made to the plaintiff was received, apparently on the theory that the evidence was relevant to the "wrongful ouster" cause of action. At the conclusion of the trial, even though the plaintiff did not seek to amend his operative pleading, the court gave certain jury instructions which were susceptible to the interpretation that the defendant Bank was obligated to make or renew loans to the plaintiff. The defendants' objections to the jury instructions given are memorialized in the record. [R.T. 15, 3043:21-3044:9; J.A. 6, 1610.] Additionally, these particular instructions were challenged by the defendants in the appellants' opening brief, and it was only natural that the instructions should be attacked as invalid, because the law recognizes no duty to make a loan, and no such legal theory had even been pleaded. [Appellants' opening brief at page 35.]

Instructional error is held to be particularly prejudicial, and to vitiate the general verdict rule, where, as in the instant case, the causes of action are interrelated and dependent upon a central set of facts. *Henderson v. Harnishfeger Corporation* 12 Cal.3d 663, 674 (1974). The entire decision rendered by the Court of Appeal is dependent upon the erroneous premise that the defendant bank had a duty to renew the plaintiff's loans. In the absence of such a duty, and the "implied" contract dreamed up by the Court of Appeal, there is simply no basis in the record for finding a breach of contract by the defendants and thereby subjecting them to liability for the alleged breach of the implied covenant of good faith and fair dealing. Similarly, only if there was a duty to renew the loans, could it be said that the newspaper coverage of the plaintiff was factually incorrect and, hence, defamatory.

It is evident from the record that, at the pertinent time, March 1987, the plaintiff was past due for one quarterly

interest payment on his $271,405.14 loan from January 30, 1987; three monthly interest payments and three and one-half months in principal on his $350,000.00 loan; three interest payments on his $63,000.00 loan, and his entire $30,000.00 loan which was due to be paid off in full on January 26, 1987. [11 J.A. 3055; R.T. 11, 2307-2318.] Under these circumstances, the printing of the factually accurate statement that the plaintiff was in default on his loans, cannot sustain the plaintiff's claim for defamation.

The two causes of action relied upon by the Court of Appeal for affirming the erroneous judgment, as well as all the other causes of action alleged by the plaintiff, cannot be sustained absent this legally untenable and factually nonexistent duty to renew a loan. The creation of such a duty and a consequent imposition of liability on the defendant Bank creates a clear conflict with the governing federal statutes enacted to ensure prudent banking practices such as were followed here. The present decision by the Court of Appeal is not only preempted by federal law, but also violates the public policy reasons which prompted the enactment of such federal law, and should be reversed by this court.

III.

Conclusion.

If there is any substance to the constitutional right to notice before forfeiture of a defendant's property, then relief should be granted to the petitioners in this case, who had no notice either in the pleadings or at trial of the cause of action pursuant to which liability has been imposed on them. Petitioners are being punished for acting prudently and in conformity with federal statutes enacted to protect innocent depositors in federally insured banks. The present Court of Appeal decision directly conflicts with the governing federal statutes, and merits intervention by this Court.

It is respectfully submitted that the Supreme Court of the United States should grant this petition for a writ of certiorari, in order to consider the issues presented. Thereafter, this Court should reverse and nullify the unconstitutional decision of the California Court of Appeal.

Respectfully submitted,

HAIGHT, BROWN & BONESTEEL,
Roy G. Weatherup, and
Rita Gunasekaran

Attorneys for Petitioners,
MICHAEL C. BILLINGS, MARYANN ARCHAMBAULT,
J. RICHARD SWARTZ, ROY E. WHITEHEAD,
and RIVERSIDE NATIONAL BANK

PROOF OF SERVICE BY MAIL

State of California

ss.

County of Los Angeles

I, the undersigned, say: I am and was at all times herein mentioned, a citizen of the United States and a resident of the County of Los Angeles, over the age of eighteen (18) years and not a party to the within action or proceeding; that my business address is 9105 Sunset Boulevard, West Hollywood, California 90069; that on April 15, 1994, I served the within *Petition For Writ of Certiorari* in said action or proceeding by depositing true copies thereof, enclosed in a sealed envelope with postage thereon fully prepaid, in the United States mail at Los Angeles, California, addressed as follows:

Clerk, United States Supreme Court
One First Street, N.E.
Washington, D.C. 20543
(By Express Mail: Original and 40 Copies)

Clerk, California Court of Appeal
Fourth Appellate District
Division Two
303 West Fifth Street
San Bernardino, California 92401

Clerk of the Superior Court
for the County of Riverside
Honorable John P. Carroll, Judge
County Courthouse
4050 Main Street
Riverside, California 92501

Clerk of the Superior Court
for the County of Riverside
Indio Branch
Honorable H. Morgan Dougherty, Judge
Department C
46-209 Oasis Street
Indio, California 92201

Mr. Roy Morrow Bell
Mr. Fletcher W. Paddison
Miller, Boyko and Bell
550 West "B" Street, Suite 400
San Diego, California 92101-3599
Attorneys for Plaintiff,
Mr. Nicholas E. Tavaglione

Superior Court Clerk
Riverside County
Post Office Box 431 -- Appeals
Riverside, California 92502

Mr. Raymond Pepper
Miller, Boyko and Bell
550 West "B" Street, Suite 400
San Diego, California 92101-3599

I declare under penalty of perjury that the foregoing is true and correct. Executed on April 15, 1994, Los Angeles, California.

Betty J. Malloy
(Original Signed)